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General Business Conditions

THE business reports during April have supplied indications that the downward trend of the past few months is finally experiencing a check. The German move into Scandinavia was the signal for a firming of commodity prices of the kind which occurred last September, although naturally much less pronounced; and in a number of industries new orders picked up. The rate of decline in industrial operations also has slackened. Steel mill activity, in which curtailment has been sharpest since December, has lost little further ground since the end of March, and is better supported by new business; and the aggregate of industrial production, as measured by composite indexes, has dropped comparatively little in April, after three months of sharp decline. According to preliminary data the Federal Reserve Board's index for the month will be 101 or 102 (1923 - 25 = 100), compared with 103 in March and a peak of 128 in December.

According to precedent, this is evidence that production and consumption are getting back into balance. With steel output below consumption during the past two months or more, steel men believe operations will be well sustained; and the steel industry is very important in this country and weighs heavily in general business indexes. Cotton print cloth mills have received needed orders, sufficient to hold off, for a time at least, the further curtailment that was threatened. Buying in non-ferrous metals picked up temporarily and reached a good volume in lead and zinc, although moderate in copper, where consumers are well covered.

Less favorable reports come from lines where unseasonably cold and wet weather has been a handicap, and this applies to a good deal of retail trade. In looking ahead account must be taken of the curtailment to be expected in automobile output during the next few months, in order to work off dealers' stocks before the end of the selling season; and some of the equipment industries are reducing backlogs and will be quieter during the Summer.

Whether the bottom has actually been reached, however, is of less importance than the indications that the decline is not feeding upon itself. Business men generally have felt that the recession would stop short of a vicious downward spiral, such as developed in 1937-38, but there have been predictions to the contrary, and they are relieved to have support for the optimistic view. It has not been easy to maintain a balanced judgment among the complexities and swift changes of the past eight months, but most business men, to their credit, have avoided excesses of either elation or fear. They sized up the dangers of the war boom in a short time, accepted the inevitability of a decline in new orders and production after the Fall uprush, and met it when it came without disappointment or panicky liquidation.

This good judgment, which keeps speculation subdued and maintains a conservative but not unduly pessimistic view, is a safeguard for the future and should be maintained, in view of war and political uncertainties. Although business has gone up the hill and down again, it is incorrect to say that it is back at the same place as at the beginning of last September, for inventories are larger and accumulated needs for capital goods have been partly satisfied. These are offsets to the fact that war business is providing support, and estimates of the outlook must take them into account.

War and Prices

To what degree the improvement in industrial orders was influenced by the spread of the war into Denmark and Norway is difficult to say. It is possible that the connection was less than it seemed, and that some improvement was due in any case. New buying has been running below consumption for four or five months, and many buyers are in position to place new commitments again, particularly where it is desirable to keep covered against war hazards. Meanwhile overproduction in certain industries, which was the chief maladjustment to be corrected, has been substantially reduced or eliminated; thus from both direc-

tions the situation has been working toward a new equilibrium.

The spread of the war is a setback for some American business, through loss of export trade and stoppage of goods actually in transit. Undoubtedly, however, the news was a factor in the firming of commodity prices. It was interpreted as signalling the outbreak of more intensive fighting and greater consumption of munitions and supplies; and the disruption of shipping and advances in ocean freight rates stimulated buying of import commodities. One of the deductions to be drawn is the likelihood that inventories will be maintained at fairly full figures.

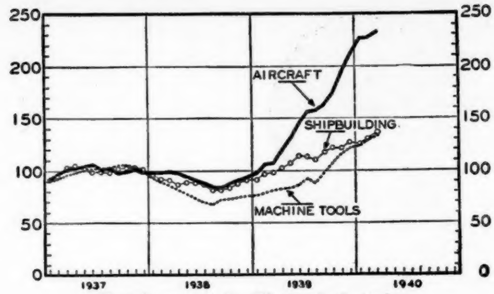
Gains in rubber are attributed chiefly to the shipping situation. Pulp and paper markets naturally strengthened. Moreover, grain and livestock prices were directly affected, partly upon the theory that the blocking of Denmark's bacon, butter and eggs from the British market would mean increased buying elsewhere, with effects reaching the United States in one way or another.

Industries Supported by War Influences

It is indisputable, of course, that the war is exerting a strong supporting influence upon business. Purchases of munitions and supplies are increasing, with another $200,000,000 aircraft order from the Allies during April and more to come. Export trade figures have continued favorable, at least up to the Scandinavian setback.

March exports totaled $352,000,000. This was a little below the $368,000,000 peak reached in December and January, but the difference is more than accounted for by raw cotton alone, which has shown the expected drop following the concentration of subsidized exports some time back. Some other agricultural exports also declined. Shipments of industrial goods have continued to expand. Sentiment will be prepared for a less favorable showing in April, in view of the tie-up of Scandinavian shipping and the interruption of exports to the Scandinavian countries.

The support given to the steel industry by export orders has been a major factor in slowing down the decline in operations. Exports of steel products, exclusive of scrap, in March were nearly three times the tonnage of a year earlier, and represented the highest percentage of steel making capacity that has been engaged in export trade since the last war. Some other industries, directly affected by war demands, are also contributing increasing support to the general situation, subject only to the limits of their capacity. The chart herewith shows indexes of employment in three of these industries, derived from figures of the Bureau of Labor Statistics and adjusted to a base of 1937 as 100.



Employment in Three Industries
(From Data of U. S. Dept. of Labor, 1937 = 100)

Although general business in the first half of 1937 was the best in seven years, it will be seen that activity in these industries is far above the levels then reached. The latest figures, for March, show that employment in aircraft manufacturing was nearly two and one-half times the 1937 average, while in shipbuilding and machine tools it was around 35 per cent larger.

The expansion of airplane manufacturing, whether measured in number of planes or value of product, has probably been greater than most people realize. At a hearing before the Senate Naval Affairs Committee on April 19, Rear Admiral John H. Towers, Chief of the Bureau of Aeronautics of the Navy, testified that the capacity of American plants is now 17,000 planes annually, and that by the end of this year we shall probably be producing at the rate of 25,000 planes annually. This compares with a pre-war plane production of around 4,000.

This increase in output is being accomplished to some extent through plant expansion, but to a greater extent by 24-hour operations, by putting a greater relative emphasis upon production than upon experimental work, and by improved mass production methods made possible by large orders.

F.H.A. Activity at Peak

Building contract awards were disappointing during the first quarter, and continued behind a year ago during the first three weeks of April, due to the low level of public works awards since the 1938 P.W.A. program ran out. However, a good seasonal improvement has developed in private residential building. The volume of new construction under Federal Housing Administration mortgage insurance has advanced steadily, setting new high records from week to week. The number of new homes started under the F.H.A. program in the week ended April 20 was 25 per cent larger than a year earlier, and mortgage insurance applications, totaling one-third more than last year, indicate further gains. The increase in construction of this type is notable through the manufacturing States along the Great Lakes and in the farm States where income

has been running high. Evidently it is a reflection of higher purchasing power and accumulated housing needs.

Farm income in the first quarter of the year, according to the Department of Agriculture, was 12 per cent above the same period of 1939. The advances in farm prices during April, particularly wheat, corn and hogs, will have a further favorable effect. Government payments, however, have declined rapidly from the levels of the Winter months, when the payments for compliance with the 1939 programs were being made. For some months ahead this source of income will be substantially smaller than heretofore.

The Spread of the War

The spread of the war into Scandinavia is another blow to international trade, paralyzing in its effects upon the peaceful and prosperous countries now invaded, and with consequences extending over the world. As trading nations the Scandinavian countries are much more important than their small populations (17,000,000 for Denmark, Norway, Sweden and Finland combined) would indicate. Their foreign trade in 1938 aggregated $2,500,000,000, a per capita average of $150 compared with only $37 for the United States. Their natural resources are small, with some exceptions, but they have abundance of a few commodities, and supply a large percentage of the world's exportable surpluses of wood pulp and paper, bacon, butter and eggs. They have one-fourth of Europe's coniferous forest area, and normally ship more than one-fourth of world exports of sawmill products, nearly three-fourths of chemical pulp exports, and one-half of paper exports. Thus their supplies are vital to other countries, and their own high standards of living rest upon a base of imports, exports and shipping.

With Denmark under German control and blockaded, Norway turned into a battleground, and Sweden and Finland bottled in, Scandinavian commerce outside the German area is cut off almost entirely; and only decisive Allied victories can restore it. Meanwhile the shifts and disruptions in other established trade channels are certain to be widespread. All shifts of trade are depressing in some quarters and stimulating in others, and the effects of the changes now occurring can be foreseen only in part. As a whole, however, they will be costly, either in the short or long run. While the battles go on exporters to the Scandinavian States are without their markets, imports which formerly came from those States, where obtainable elsewhere, are more expensive, and the interruption of shipping is aggravated. All these are costly offsets to the gains of shippers or domestic industries who receive business diverted from Scandinavia, and to any increased demands for munitions and supplies that may reach this country.

U. S. Trade with Scandinavia

The Scandinavian countries are valued customers of the United States. Historically they have bought from us more than they sold to us, covering the difference by shipping and tourist receipts, and by transfers from London out of the proceeds of their excess of exports to Great Britain. Our exports to the four countries in the twelve months before the war were about equal to exports to Germany, and since the war began they have expanded sharply, in part making up our loss of German trade. From September to February inclusive they aggregated $115,000,000. Our imports from the same countries were $51,000,000.

At this rate an export trade exceeding $200,000,000 annually, or about 5 per cent of our total exports, and an import trade almost half as large, are at stake. The automobile and allied industries will feel the loss most seriously; the majority of cars sold in Scandinavia are of American make, and American assembly plants are located in Denmark and Sweden. Some 20 per cent of our exports have been motor vehicles, and another 15 per cent gasoline and other petroleum products. Other important shipments include machinery and raw cotton, and since the rearmament race started the United States has furnished an unusual proportion of the steel, particularly wire, imported by these countries.

Among United States purchases from Scandinavia wood pulp and paper predominate, constituting 80 to 90 per cent of our imports from Sweden and Finland and one-fourth of our imports from Norway, which also ships us fish products and fertilizers. Imports from Denmark are small and chiefly agricultural specialties.

The Wood Pulp Situation

United States imports of wood pulp normally total around one-fifth of domestic consumption, and about 70 per cent of the imports come from Scandinavia, chiefly unbleached sulphite and unbleached sulphate. In 1939 one-half of the United States consumption of unbleached sulphite, which totaled 1,360,000 tons, was supplied by imports. Of the 3,000,000 tons of unbleached sulphate used, over one-sixth was imported.

According to the 1939 report of the United States Pulp Producers Association, domestic capacity for pulp production (all kinds combined) is adequate for domestic consumption. However, unbleached sulphite capacity, considered separately, falls about 20 per cent short of domestic needs. In any case suspension of imports from Scandinavia will lead to increased demands upon U. S. and Canadian mills and pulpwood supplies, not only from domestic requirements but possibly from other countries which have relied upon Scandinavian pulp and paper. The pulp market has strengthened accordingly. While quotations are largely nom-

inal, foreign unbleached sulphite is quoted $65 to $75, against $55 to $60 before the invasion, and other pulps are up in proportion. Domestic pulp is sold on quarterly contract prices, the open market is small, and readjustments therefore take place slowly. There may be reason to be thankful for the construction of pulp mills in the South during the past few years. Since 1936 approximately 3,000,000 tons of new capacity, largely for making sulphate pulp used in kraft papers, have been installed in the country.

The supply of pulp for rayon manufacture is not directly affected by the European developments. None of this high grade pulp is imported from Scandinavia. In 1939 we imported 88,000 tons from Canada and exported 48,000 tons. Domestic consumption was 200,000. Calculated domestic capacity is 336,000 tons, and although rayon output broke all records this branch of the pulp industry operated at less than 50 per cent of capacity.

Only a small fraction of our imports of newsprint come from Europe, and within the past month the Canadian contract price of $50 has been extended unchanged for the third quarter.

Britain Loses Sources of Supply

Upon British trade particularly, the repercussions of the spread of war will be more serious than upon the United States. Great Britain covered nearly 90 per cent of her pulp requirements, and about 44 per cent in value of her paper imports, from the Scandinavian countries. Earlier in the war she had lost minor sources of supply, when Poland and the Eastern Baltic States became inaccessible. She has turned chiefly to Canada and Newfoundland to make good some of the losses, and has taken steps to restrict both timber and paper consumption and to develop substitute materials.

Equally important to Great Britain have been the pork and dairy products imported from Scandinavia, chiefly Denmark. The agriculture of Denmark is, in effect, a factory system, scientific and largely cooperative, which converts imported feedstuffs—Argentine corn, Brazilian cottonseed cake, Danubian sunflower seed cake—into high quality pork and dairy products for export. The basic dairy product, milk, is processed into butter; the by-product, skimmed milk, is fed to pigs to produce high quality bacon. Denmark alone shipped nearly one-half of the world's export of bacon in 1937, and together with other Scandinavian countries about 26 per cent of world butter exports and about one-half of fresh egg shipments.

Great Britain purchased a large share of her requirements in these countries—in 1938 53 per cent of her bacon imports, over 30 per cent of her butter and nearly 40 per cent of her egg imports. Thus she will have to ration consumers more closely, or turn to other markets. American business is concerned to know whether she will buy in the United States, particularly pork products, prices of which are on an export basis.

Doubtless the British will confine their bacon purchases as far as possible to Canada, conserving their dollar exchange to pay for munitions. However, demands in time may overflow into the United States. For the present no increase in British buying is expected. The Food Ministry has announced that heavy pork stocks now on hand must be reduced before hot weather, British and Irish bacon production is larger than counted on, and consumption is expected to be reduced. Whatever the outcome, there will be no change for the present in the quota limitation which Canada placed on February 26 on her imports of pork from the United States. This quota is 1,626,769 pounds monthly, equal to the average of the first nine months of 1939, but only one-sixth of the January total.

American butter cannot be sold in Great Britain unless the British Government should decide to pay an import subsidy, for the American price, which is supported by U. S. Government purchases, is substantially above an export basis and approximately equal to the fixed price in Great Britain. Thus there is no margin to cover shipping costs and the British duty of about 2⅝ cents on non-Empire butter. Where Britain will replace her Danish butter supplies remains to be seen. Doubtless consumption will be reduced and use of margarine and cheaper cooking fats increased, which may raise her requirements for other oils.

Further Disruption of Shipping

At best, the spread of the war will necessitate longer hauls for about 10 per cent of British imports. The confusion about the legal status of the Norwegian and Danish merchant fleets, which immediately disrupted their service on international trade routes, is still but partly cleared up. The Danish fleet, which consisted of some 700 vessels (100 tons or more) of 1,175,000 gross tonnage at the beginning of 1939, is now off the high seas, considered a "technical enemy" by the Allies unless transferred to the Allied flag. The Norwegian fleet, which early in 1939 numbered 1,987 ships totaling 4,833,000 gross tons, has been placed at the disposal of the Allies, who have restricted its movements considerably. Late in the month, however, the restrictions were eased somewhat permitting Norwegian ships to return to the Cuban and Chilean trades. The Swedish merchant fleet has been ordered out of the war zone.

According to the United States Maritime Commission, 47 Danish and Norwegian vessels have been operating regularly on routes between this country, South America and the Far East. At present there are not enough American vessels available to take their place, although 117 vessels owned by the Maritime

Commission are still laid up. Most of these ships are more than twenty years old; under the present law, it will require Congressional consent to permit their being chartered, and a joint resolution to that effect is now pending.

As the war proceeds the strain on shipping facilities tightens. Tonnage on many routes has been reduced by the diversion of British ships to war services, withdrawal of American ships from combat areas, and the laying up of the German merchant fleet. Moreover, the convoy system is said to have diminished the efficiency of the British merchant marine by half. War losses themselves have been relatively small, amounting to about 2.5 per cent of world shipping, and have been partly offset by the construction of new ships, which in Great Britain is approaching a mass production basis.

The decrease in shipping space has been reflected in the rise of freight rates, which since the beginning of the war have advanced 100 to 500 per cent, in some cases, on routes to the war zone. As a whole, however, the ocean freight rate structure is far below the World War levels. It is estimated that the rates of conference carriers represent only about 15 per cent of the peak then reached, while charter rates have fluctuated up to about one-half of the 1914-18 top.

As a group the Scandinavian countries owned early in 1939 roughly 8,000,000 gross tons of shipping, or about 12 per cent of the world fleet. A distinctive feature of their shipping was the large number of vessels designed for special trades. Of the total Norwegian tonnage in 1937, for example, tankers represented 43 per cent. Other specialties were the Norwegian and Danish fruit carriers and the Norwegian whaling fleet. The net earnings of these fleets, which amounted to about $220,000,000 in 1937, have been a major factor in the balances of payments of the Scandinavian countries. Together with tourist income, which brought in a net of about $30,000,000 in the same year, they have served to pay for the excess of imports and for debt service.

Striking at the Source of Scandinavian Prosperity

To the Scandinavian countries themselves the spread of hostilities is a tragedy whose extent cannot yet be determined. The effects of war are nowhere so demoralizing, disrupting and utterly devastating as when they fall upon countries whose economic life is based to a high degree upon peaceful trade and exchange of services with other countries. Deprived of these exchanges, the high standard of living and stable prosperity which the Scandinavian countries have enjoyed up to the outbreak of war will be stricken at the source. The Danish agricultural system, based upon the import of foreign feedstuffs and their manufacture through the livestock industries into high quality products for export, seems likely to be gravely disrupted; and to the extent that the supply of feed is reduced liquidation of livestock, the basic productive asset of the country, is threatened. To what extent the Norwegian fishing fleet and canneries will be handicapped remains to be seen. Operations of the mines and wood-manufacturing industries, less dependent on foreign materials, will be less hampered, but the question is of markets, as long as ports are closed and transportation disrupted.

The situation may change, but as it stands Germany now has control of greater food supplies in Denmark and access to a greater share of whatever exportable surpluses the other countries may produce under war conditions. But what she can give in return, and whether the present high productivity of Scandinavian agriculture and industries can be maintained, without access to international markets, are other questions; and unfortunately the answer must be expected to be unfavorable in its implications for the Scandinavian economy.

The War and the Foreign Exchanges

The spread of the war to Scandinavian countries has introduced new problems and complexities into the foreign exchange situation.

On April 9, immediately following the invasion of Denmark and Norway, banks here and in other leading exchange centers suspended dealings in Danish and Norwegian currencies save in cases of definitely ascertained legitimate needs of customers. On the next day President Roosevelt, by executive decree, ordered the "freezing" of all Danish and Norwegian balances in this country, prohibiting all transfers from these accounts except as specifically approved by the United States Treasury. Later this order was interpreted as applying to securities as well as to other assets. In making this move, the Government evidently was prompted by a desire to protect banks and other fiduciary institutions against legal risks where authority to make transfers might be in doubt, and also by a wish to safeguard Danish and Norwegian holdings against falling into unauthorized hands.

Trading in Swedish exchange was greatly curtailed owing both to lack of demand and to the policy of the Swedish authorities of controlling capital exports. The krona dropped nearly half a cent to a new low of 23.40 cents, later recovering most of this loss.

Scandinavian Gold Reserves and Other Funds

With the extension of German control over Denmark and parts of Norway, interest has been aroused as to the status of the gold reserves of those countries and of Sweden. The following table gives latest available figures on gold and foreign exchange holdings of the central banks of the three countries, together

with comparative figures at the end of 1938, and by months since the outbreak of war last September.

Gold & Foreign Exchange Holdings of Scandinavian Countries

(All Figures in Millions of Dollars)

	Sweden		Norway		Denmark		Total	
Date	Gold	Fgn. Exch.	Gold	Fgn. Exch.	Gold	Fgn. Exch.	Gold	Fgn. Exch.
Dec. 1938....	321	181	94	24	53	23	468	228
Aug. 1939....	355	132	107	30	53	2	515	164
Sept. "	357	113	107	18	53	2	517	133
Oct. "	332	100	103	18	53	2	488	120
Nov. "	333	92	103	21	53	2	489	115
Dec. "	308	72	94	22	53	2	455	96
Jan. 1940....	258	97	84	23	53	2	395	122
Feb. "	218	115	84	20	53	2	355	137
Mar. "	173	134	84	20	53	2	310	156

Note: Foreign exchange holdings converted at prevailing rates of exchange.

The fourth Scandinavian country, Finland, held about $64,000,000 of gold and foreign exchange in its central bank prior to the Russian invasion, but since then publication of figures has been discontinued.

It will be seen that the three countries had at the end of March combined holdings of $310,000,000 of gold, plus about $156,000,000 in foreign exchange assets. Compared with the end of 1938, gold holdings were down by about $158,000,000 and foreign exchange by about $72,000,000, most of these losses having occurred since September when the drain due to flight of capital, payments for emergency reserves of commodities and war materials, and the general dislocation of international payments became more acute.

Of gold still in the possession of Scandinavian countries, a good part is understood to be located abroad, principally in the United States. For some time these countries, like others in the war zone, have been known to be shifting their gold reserves to places of greater safety. Official figures as to the size of these foreign holdings are lacking, but it is significant that from the outbreak of European hostilities last September to the middle of April our gold imports have included $152,000,000 from Sweden, $44,000,000 from Norway and $5,000,000 from Denmark. According to unofficial reports, the bulk of the Danish gold has been deposited in London, while gold remaining in Norway at the time of the German invasion is said to have been removed to a safe place.

Besides their gold reserves, the above three Scandinavian countries had here at the end of January cash balances aggregating in all $258,000,000, distributed as follows: Sweden $162,000,000, Norway $67,000,000 and Denmark $29,000,000.

Moreover, to complete the record, mention should be made of credits authorized to these countries through the Export-Import Bank this year, consisting of $10,000,000 each for Norway and Denmark, $15,000,000 for Sweden and $1,000,000 for Iceland. Except for a small amount in the case of Norway, none of these credits has been utilized. To what extent they may be affected by recent developments is not clear at this time.

Effects on Other Exchanges

Outside the Scandinavian area, the effect of this new eruption of the war front has been to increase the general state of alarm regarding European conditions and to intensify pressure upon the exchanges, particularly those of neutrals contiguous with Germany.

While official rates for sterling, covering the bulk of transactions, remained steady at the buying and selling spread of $4.02½-$4.03½, the open market or free rate dropped to a new low at $3.43½ on news of the Scandinavian affair, closing the month around $3.51. The market continues highly erratic, movements depending a great deal upon the character of war news.

In spite of increased pressure, guilders and Swiss francs remained steady due to support by exchange controls. Belgas, on the other hand, declined from 17.11 cents at the beginning of the month to a low of 16.73, later recovering to around 16.90.

Canadian free exchange moved contrary to the general run of rates, rising from a discount against U. S. dollars of about 18½ per cent at the beginning of the month to a high of 13½ per cent on April 16. Subsequently the market reacted to around 15 per cent discount and held in that neighborhood for the balance of the month. The official rate has continued at approximately 10 per cent discount, as established in March.

Discussing the open market for Canadian funds in New York, Governor Towers of the Bank of Canada recently stated that transactions in this market probably do not include more than 1 or 2 per cent of total Canadian exchange transactions. In this connection he said:

> The rate in this open market in the United States is the rate at which non-resident owners of Canadian dollar balances are prepared to sell them to other non-residents. For example, if one United States resident with a Canadian dollar balance wishes to dispose of it to another United States resident, they agree between themselves, or through the medium of a United States bank, at what price in United States dollars they wish to make the transfer, and the price so agreed becomes the transaction in the unofficial market.
>
> The volume of transactions in this market is very small, perhaps not more than 1 or 2 per cent of total Canadian exchange transactions. The board (Canadian Foreign Exchange Board) has no direct contact with this market, and no influence on rates, and as Canadian dollars bought in the unofficial market cannot be used to pay for Canadian exports, the demand for such dollars is limited. Thus, non-residents who wish to sell have not found many buyers and have had to offer Canadian dollars down until they reached a point at which buyers were attracted.

> When the unofficial rate for the Canadian dollar in New York suffered a sharp fall in March, I believe some people were disturbed because they thought that this decline had some meaning in respect to the official rate. It had no such significance. What it did mean was that one non-resident, Tom Jones, got worried about his Canadian balances and decided to cut the price to sell them to John Smith, another non-resident.

Recent firmness in the Canadian free rate coincides with the opening of the shipping season at Canadian ports, and is therefore in accordance with the normal seasonal tendency.

Broadly speaking, Canada's problem of financing her external trade under war conditions is that of finding U. S. dollars to pay for her increasing imports from the United States when a growing proportion of her exports are in sterling due to her large sales to Great Britain. In a recent move to relieve this situation, the Canadian Foreign Exchange Control Board has ruled that henceforth all imports *through* the United States, as in the case of rubber, wool, jute, tin and others, will be paid for in the currency of the country of origin instead of in United States dollars, thus enabling the Dominion to utilize sterling for these purposes and to conserve its supply of United States currency. Also, the Canadian authorities are counting upon a considerable gain in tourist trade from the United States during the Summer, owing to the war which has debarred visitors to Europe.

The Situation in Sterling

Referring again to sterling, it is noteworthy that one effect of the tightening of the exchange control has been to make New York the leading foreign exchange market of the world. Because London, and the British Empire generally, no longer deal in free exchange, but only in official exchange, the greater part of the business of Latin America, Asia and continental Europe that formerly went to London, now comes here. To a much smaller extent business has been diverted to Holland and Switzerland.

The principal source of free sterling under present conditions is foreign-owned balances in London created either before the war or more recently from the proceeds of British imports invoiced in sterling. Of the latter there seems to be an increasing amount. Just why this should be so is not clear, except that for some reason import permits seem to be easier to obtain where payment is to be made in sterling.

An indication of the attitude of the British authorities towards fluctuations in sterling was afforded by the Chancellor of the Exchequer on April 9. Referring to the decline that had taken place in foreign centers, Sir John Simon expressed the view that it would be wrong to interfere in support of sterling in the free market. While alive to the fact that each successive decline in the unofficial rate was a strong inducement to avoidance of the official market and to further depreciation of sterling, the Government, he said, rejected blocking of foreign assets as running counter to liberties and traditions that had made London an attractive banking center to foreigners. Asserting that the amounts involved in the free market were small and that the bulk of the foreign exchange business was done at the official rate, which had been maintained at a virtually stable level ever since the beginning of the war, the Chancellor continued, "That may have the result that any outside market for sterling becomes very thin, and a thin market is always erratic. If our general policy is sound, as I am convinced it is, we must not be deflected by secondary considerations."

The Question of Trade Competition

The decline in the rate for free sterling has given rise to anxiety on the part of some merchants and manufacturers who have to compete with British goods in this and foreign markets. However, in considering the possible effects of sterling depreciation, many factors need to be taken into account. In the first place, not all British products can be paid for in free sterling. According to the exchange regulations, an important list of Empire products—rubber, tin and tin ore, jute and jute products, whiskey and furs, together with all Australian exports, including wool—must be paid for in "official" sterling, hence are not affected by what happens in the free market.

While available statistics do not permit of precise comparisons, it has been estimated very roughly on the basis of 1938 figures that about 13½ per cent of United Kingdom exports are payable in official sterling; India, Burma and Ceylon about 53½ per cent; and Malaya about 88½ per cent. Taking United States imports alone from the above areas, similar rough calculations based on 1937 and 1938 figures suggest that about 33 per cent of our imports from the United Kingdom (chiefly whiskey) will have to be paid for at the official rate; India about 54 per cent (jute and burlap); Ceylon about 65 per cent (rubber); and Malaya about 95 per cent (mostly rubber and tin).

To the extent that our goods compete with British goods payable in free sterling, the exchange rate is of course an influence, though not necessarily a decisive one. For one thing, British internal prices, according to standard indexes, have risen about 30 per cent since the start of the war, offsetting in part at least the decline in sterling. High freight rates and shipping difficulties are other considerations. And finally there is the question of Britain's capacity to expand her exports at a time when the demands upon her industries and manpower for carrying on the war are so great.

How these various factors will work out in the long run remains to be seen, but certainly there has been little evidence so far of broadly harmful consequences to our trade. As recently pointed out by Secretary Hull, our exports to Great Britain since the outbreak of war have increased far more than our imports from that quarter. In the leading South American market — Argentina — figures covering the first three months of the year indicate that we displaced Great Britain as the number 1 supplier, our shipments almost doubling as compared with the same period last year.

Nevertheless, the fear of exchange dumping persists; prompting the Treasury last month to rule that imports into this country be valued for customs purposes at official rather than free rates, the regulations to apply not only to sterling, but also to the Canadian dollar, the Newfoundland dollar and the Australian pound. Considering all that has been said of the "folly" of trading our products and services for "useless" gold "to bury in Kentucky," it might perhaps have been thought that the country would be willing to accept some larger measure of payment in usable and consumable goods, but evidently such is not the case. Apparently we must go on buying gold if we are to maintain our exports, since we are unwilling also to grant credits.

British Trade Policy

That the British will strive in every way practicable to maintain and expand their foreign trade in order to conserve their vital holdings of gold and foreign exchange may be taken for granted. The official White Paper issued on March 5, 1940 by the recently established Export Council states frankly that "the maintenance of export trade is so vital a factor in the war effort of the Allied Powers that no measure calculated to contribute to the end in view should be excluded from consideration." This is plain speaking, but clearly the situation, as revealed by the trade figures, is urgent, imports continuing to run heavily above exports, with the March trade deficit double that of March a year ago and the largest for any month since 1929. The announcement by the British Government last month requisitioning the second lot of dollar securities from British investors for sale in this country is a further reminder of the drain being imposed upon the national resources.

In the discussion that has been going on in Great Britain as to the methods of expanding trade, it is interesting to find two of London's leading financial weeklies, The Statist and The Economist, taking the position that currency depreciation at this juncture could only have harmful results. "Any attempt," says The Statist on February 24, "to stimulate exports by the orthodox method of currency depreciation would clearly be suicidal at a time when we are over-importing heavily, since this would be merely to turn the terms of trade against us," while The Economist of April 9 asserts that any further devaluation would be harmful on the ground that "it is in our interest in war-time to keep the value of our currency as high as possible, so that we can buy cheap and sell dear."

As the Allied Powers must pay cash for supplies in this country, they naturally husband their cash resources for purchases here of war supplies unobtainable elsewhere. For the same reason they are intensifying their efforts both to become more self-sufficient at home and to extend trade ties with other countries, where it is possible to arrange for mutual exchange of products. To the extent that such efforts are successful they mean increased competition for our exporters, and, perhaps more important, the creation of new economic ties that may outlast the war, and thus narrow the area of free competition.

The opinion of above quoted British authorities that further depreciation of sterling is undesirable, solely in their own interest, is something to be considered by American business men who fear intensified British competition. While the war lasts and the Allied Powers have gold and dollar balances to draw upon, a high level of aggregate exports from the United States seems assured. Thus the danger is not of an immediate shrinkage in our overseas business but rather that it may become too heavily dependent upon war stimulated demands, with consequent difficulties should Allied purchasing power become exhausted or when the war comes to an end.

Money and Banking

In the domestic money market, news of the outburst of active fighting in Europe was taken calmly. Short-term money rates, as expected, showed no change whatsoever, having long ago lost all sensitivity under the overwhelming surplus of available funds. More significant was the behavior of the bond market, where losses in high grade issues were moderate and generally within a range of 1 or 2 points at the most, followed in many instances by substantial recoveries. The showing contrasts with the severe disturbance of market conditions produced by the outbreak of war last September.

Two factors seem to have been mainly responsible for the good performance of the market during the month, viz., (1) the existence all along of apprehensions of an intensification of active warfare, so that the market was to a certain extent prepared for the event in advance, and (2) the constantly increasing supply of excess funds held by the banks.

As to the latter, in the four weeks ending April 24 the excess reserves of member banks

increased by no less than $440,000,000 to the record high of $6,120,000,000. Nor is there any likelihood of an early turn in the trend, for the reason that the inflow of gold which has been the major factor in creating excess reserves seems destined to continue. This obviously has an important bearing upon the question of the future of interest rates. So long as the supply of surplus funds is not only unprecedentedly large, but still increasing, it constitutes a powerful influence in support of easy money.

Condition statements of weekly reporting banks revealed institutions in New York City to have been substantial purchasers of Treasury bonds during the interval of market softness in the early part of the month. Later there was a tendency to shift out of Treasurys into guaranteed issues and notes. Outside New York City, reporting banks as a class reduced their holdings of direct Treasury bonds during the period. Loans of the reporting system for business purposes, including term loans, continued to work gradually higher, reaching a new peak since January, 1938, up $135,000,000 from the January low of this year and approximately $570,000,000 above the levels of April last year. Recent totals, however, were still some $450,-000,000, or about 10 per cent, under the October high of the 1937 business recovery.

New corporate financing last month was in good volume, aggregating approximately $260, 000,000. Of this amount, about $200,000,000 represented refinancing and $60,000,000 new capital, the latter making the best showing for any month since April a year ago. Besides the pick-up in offerings representing new money, an encouraging feature was the marked increase in equity financing, total preferred and common stock offerings reaching an aggregate of $75,000,000, the largest for any month in nearly three years. In general the new issues during the month were well received.

A Criticism of Cheap Money Policies

In the annual report of the Federal Reserve Board for 1939, made public within the past month, it is disclosed for the first time that on three separate occasions last year the Federal Advisory Council protested to the Board against what it termed the policy of "extreme easy money." The Council, which is provided for in the Federal Reserve Act, serves in a purely advisory capacity; nevertheless its deliberations and recommendations command respect by virtue of its membership, consisting of a leading business representative from each of the twelve Federal Reserve districts, whose selection has been determined upon by the boards of directors of the Reserve Banks of those districts. Included in the membership of the Council in 1939 were Walter W. Smith, president of the First National Bank in St. Louis; Howard A. Loeb, chairman of the Tradesmens National Bank & Trust Co., Philadelphia; Leon Fraser, president of The First National Bank of New York; Robert M. Hanes, president of the Wachovia Bank and Trust Co., Winston-Salem, N. C.; Thomas M. Steele, president of the First National Bank and Trust Co. of New Haven, Conn., and Edward E. Brown, president of The First National Bank of Chicago.

While space considerations prevent a full statement, it is possible to summarize certain of the principal points briefly, as follows:

1. Though the easy money policy has been followed since 1929 on the theory that it would stimulate business and cause business to borrow and banks to lend, it has done neither; but rather has done and is doing undeniable economic injury to the whole savings class of the American people.
2. It is reducing the income of schools, colleges, churches, hospitals and educational and charitable institutions of all kinds dependent upon endowments, forcing more and more of their functions to be taken over by public boards at the expense of the taxpayer.
3. Through failure to bring to the banks normal rates on loans and investments, it is tending to weaken the capital position of the banks and is encouraging an unhealthy position of bond portfolios through the inducement towards long maturities at progressively lower rates.
4. By lessening the current cost of government financing, it has made the people, and even Congress itself, indifferent to the steadily mounting government debt and is tending to create illusions as to the eventual burden of carrying a constantly increasing debt.

Asserting that "a prolongation of this situation threatens the existence of private banking and with it the whole system of private enterprise," the Council yet recognizes that "the long continued easy money policy has created a condition the correction of which can only be gradually attained." It concludes with the request that the Board, "as one of the greatest single services which it can render to the country as a whole," bring about a modification of the policy of "extreme easy money."

The warning by the Federal Advisory Council is both timely and well-founded. Certainly cheap money has proved to be no panacea against unemployment and depression. To be sure, doubts may exist as to how far the Reserve Banks have been in a position to alter conditions, assuming they wished to do so, for during recent years at least gold imports have been the major cause of the towering excess reserves that have depressed interest rates. With gold still pouring into the country and no end to the movement in sight, the situation evidently affords no easy solution. The Council, however, has performed a service in calling attention to the problem and in stressing the dangers inherent in prolonged periods of abnormally easy money.

First Quarter Profits

Earnings of leading industrial companies for the first quarter of this year were moderately below those of the fourth quarter of 1939, but

well above the first quarter of 1939, when business generally was at a much lower level and many companies operated at a deficit or on the borderline of profits. A tabulation of the reports issued by 340 companies for the quarter ended March 1940 gives combined net profits, after taxes and less deficits, of approximately $336,000,000. This shows a decrease of 18 per cent from the $408,000,000 reported by the same companies in the December 1939 quarter, but an increase of 74 per cent over the $193,000,000 total in the March 1939 quarter.

Net worth of the group aggregated $11,800,000,000 at the beginning of this year, upon which the first quarter profits were at the annual rate of 11.4 per cent, against a 6.6 per cent rate of return upon a slightly smaller net worth in the first quarter last year. Comparative figures are given in the accompanying summary, classified by major industrial groups. As pointed out heretofore, the published reports of a limited number of large companies indicate the trend of earnings, but not the average rate of earnings for business as a whole; the latter may be obtained only from the annual "Statistics of Income," compiled and issued some time later by the Treasury Department.

An examination of our summary will show that the increases in first quarter profits as compared with last year were quite general, but that the sharpest gains were registered in such lines as metals, machinery and equipment, paper and petroleum, in which earnings a year ago were still at a relatively low level. A number of representative companies in certain lines, however, had the largest first quarter earnings in their history. In the steel industry, the rate of operations, although down from the peak reached last December, was much higher than in the initial quarter of 1939, with resultant lowering of unit costs and widening of profit margins. Substantial increases in sales and profits were shown by a majority of the leading manufacturers of machinery, electrical equipment, railway equipment and numerous other metal products, although in some cases the percentage gains tend to exaggerate the degree of improvement because of the low base from which they are figured. Sales and earnings of leading automobile companies were higher, and manufacturers of automobile parts and equipment are working also on large orders from the aircraft industry.

In the group of related industries producing pulp, paper and the various paper and paperboard products, there naturally has been an increase in demand due to the higher level of general business activity this year, but at the same time the customary supply of imported pulp and paper has been severely curtailed by the war. Prices have advanced sharply, and recent earnings of many representative companies have been lifted to the highest level in several years. In the oil industry, the marked increase in first quarter earnings reflected the improvement in marketing conditions and bet-

PROFITS OF LEADING CORPORATIONS FOR THE FIRST QUARTER

Net Profits Are as Reported, After Depreciation, Interest, Taxes, and Other Charges and Reserves, but Before Dividends.—Net Worth Includes Book Value of Outstanding Preferred and Common Stock and Surplus Account at Beginning of Each Year.

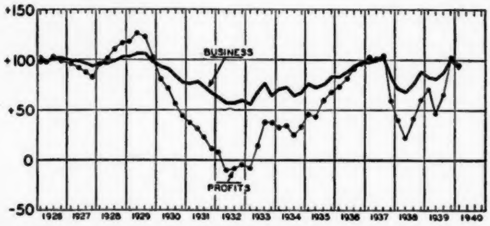
(In Thousands of Dollars)

No.	Industrial Groups	Net Profits First Quarter 1939	Net Profits First Quarter 1940	Per Cent Change†	Net Worth January 1 1939	Net Worth January 1 1940	Annual Rate of Return % 1939	Annual Rate of Return % 1940
6	Food—baking	$ 4,322	$ 4,091	— 5.3	$223,344	$220,401	7.7	7.4
17	Food products—misc.	18,159	20,091	+10.6	643,422	652,624	11.4	12.3
12	Textiles and apparel	3,928	5,255	+33.8	114,121	122,314	13.8	17.2
15	Paper products	1,471	4,565	+	185,937	198,202	3.2	9.2
24	Chemicals, drugs, etc.	42,239	56,980	+34.9	1,359,629	1,407,748	12.4	16.2
12	Petroleum products	5,186	29,611	+	1,373,740	1,392,237	1.5	8.5
16	Stone, clay and glass	5,166	7,189	+39.2	349,068	354,329	6.0	8.1
1	Iron & steel—U. S. Steel	661	17,114	+	1,298,907	1,314,807	0.2	5.2
27	Iron & steel—other	6,153	32,088	+	1,501,894	1,538,894	1.6	8.4
6	Metal—building equipment	586	3,020	+	195,258	187,725	1.2	6.4
12	Metal—electrical equipment	10,016	18,466	+84.4	553,604	563,892	7.2	13.1
25	Metal—machinery	1,653	3,958	+	104,644	108,229	6.4	14.6
7	Metal—office equipment	3,643	4,253	+16.7	134,051	135,699	10.9	12.5
10	Metal—railway equipment	509	5,688	+	182,095	174,003	1.1	13.1
34	Metal products—misc.	6,314	10,855	+71.9	308,867	316,399	8.2	13.7
1	Automobile—Gen. Motors	53,178	67,028	+26.0	1,027,817	1,053,560	20.7	25.4
6	Automobile—other	663	2,033	+	104,541	108,057	2.5	7.5
23	Auto equipment	8,015	13,675	+70.6	234,782	248,319	13.6	22.0
25	Misc. manufacturing	4,604	6,057	+31.6	316,865	313,668	5.8	7.7
279	Total manufacturing	176,466	312,017	+76.8	10,212,586	10,411,107	6.9	12.0
10	Mining—coal	D-783*	1,245*	+	215,156	200,314	......	2.5
15	Mining—metal	10,545*	12,683*	+20.3	676,797	682,300	6.2	7.4
9	Mining & quarrying—misc.	4,453*	5,305*	+19.1	176,413	177,057	10.1	12.0
13	Trade	239	1,841	+	173,728	167,746	0.6	4.4
14	Service & construction	2,367	2,816	+19.0	158,348	161,653	6.0	7.0
340	Total	$193,287	$335,907	+73.8	$11,613,028	$11,800,177	6.6	11.4

D- Deficit. * Before certain charges. † Increases or decreases of more than 100 per cent not computed.

ter spread between prices of refined products and costs for crude oil, operating expenses and taxes, which began to develop in the latter part of 1939, plus unusually heavy consumption of fuel oil this season.

The longer term trend of industrial profits is indicated by the accompanying chart, which is based upon the rate of return on net worth of 200 large corporations and is adjusted for seasonal variation.



Quarterly Index of Industrial Corporation Profits and The Annalist Index of Business Activity. 1926 = 100.

Preliminary figures for the first quarter show that business activity and profits were only moderately below those of the preceding quarter, or of the best quarters of 1936-1937. Even in those two years, however, the official statistics for all corporations in the United States (approximately 478,000) show that the number of active corporations reporting no net income made up 58 per cent and 60 per cent, respectively, of the total number.

Change in First Quarter Sales

The following table giving the percentage change in first quarter sales, 1939-40, of 40 large manufacturing companies and an equal number of retail trade organizations will show the highly uneven character of the gains this year.

Aggregate sales of the manufacturing group increased from $952,000,000 to $1,150,000,000 or by 21 per cent. These figures are based upon shipments or "sales billed," which in the first quarter of this year doubtless were in many instances larger than new orders received or "sales booked" during the same period, inasmuch as many companies were working off heavy back-logs of unfilled orders taken during the wave of buying last Fall. The chain store, department store and mail-order group had an increase in aggregate sales from $746,000,000 to $828,000,000, or 11 per cent.

Railway and Utility Earnings

Railroad freight and passenger traffic during the first quarter declined seasonally from the high levels of the final 1939 quarter, but gross operating revenues of the class 1 systems were about 10 per cent above those of a year ago,

% Change in First Quarter Sales, 1939-1940

Manufacturing		Trade	
Abbott Laboratories	+18.1	American Stores Co.	+13.3
Air Reduction Company	+26.5	Barker Bros. Corp.	— 1.1
American Radiator Co.	+ 9.7	Bond Stores	+39.3
Atlantic Refining Co.	+20.7	Consol. Retail Stores	+ 8.6
Atlas Powder Co.	+22.6	Crown Drug Co.	+ 7.7
Beatrice Creamery Co.	+21.0	Dixie-Home Stores	+14.9
Caterpillar Tractor Co.	+13.1	Edison Bros. Stores	+13.4
Colorado Fuel & Iron	+39.8	Marshall Field & Co.	+11.9
Crown Cork & Seal Co.	+24.0	M. H. Fishman Co.	+12.2
Curtis Publishing Co.	+ 6.8	Grand Union Co.	+ 6.2
E. I. du Pont & Co.	+17.7	W. T. Grant Co.	+ 9.2
Flintkote Company	+ 9.8	H. L. Green Co.	+11.3
General Electric Co.	+25.4	Interstate Dept. Stores	+ 7.0
General Foods Corp.	+10.8	Jewel Tea Co.	+ 9.9
General Motors Corp.	+24.6	S. S. Kresge Co.	+ 8.7
General Time Inst.	+22.2	S. H. Kress & Co.	+10.0
Hazel-Atlas Glass Co.	+ 5.4	Kroger Groc. & Bak.	+ 6.8
Hercules Powder Co.	+38.1	Lane Bryant, Inc.	+ 1.8
Hinde & Dausch Paper	+12.1	Lerner Stores Corp.	+13.2
Interlake Iron Corp.	+23.2	McCrory Stores Corp.	+14.0
Johns-Manville Corp.	+13.7	Melville Shoe Corp.	— 0.4
Kimberly-Clark Corp.	+ 4.8	Montgomery Ward	+16.3
Link-Belt Co.	+34.6	G. C. Murphy Co.	+19.0
Lone Star Cement	— 3.4	Natl. Tea Company	+14.6
Mead Corporation	+18.5	Neisner Bros., Inc.	+14.8
Natl. Cash Register	+ 6.2	J. J. Newberry Co.	+13.6
Ohio Oil Co.	+22.2	J. C. Penney Co.	+11.8
Otis Elevator Co.	+14.8	Peoples Drug Stores	+ 5.2
Pittsburgh Steel Co.	+30.3	Rand's Inc.	+14.2
Quaker State Oil Ref.	+39.7	Reliable Stores Corp.	+20.4
Ruberoid Company	+15.7	Rose's 5-10-25c Stores	+21.0
Scott Paper Co.	+26.4	Safeway Stores, Inc.	+ 6.3
Sharon Steel Corp.	+48.5	Schiff Company	+ 8.5
Shell Union Oil Corp.	+16.5	Sears, Roebuck & Co.	+11.5
Skelly Oil Co.	+ 9.3	Spiegel, Inc.	+15.3
Standard Brands	+ 0.1	Sterchi Brothers	+ 6.7
Tide Water Assoc. Oil	+17.0	Union Premier Food	+34.9
United Aircraft Corp.	+70.6	Walgreen Company	+ 5.4
Westinghouse Electric	+24.6	Western Auto Supply	+21.9
Wheeling Steel Corp.	+ 3.3	F. W. Woolworth Co.	+10.6

while net railway operating income increased by about 34 per cent, despite heavier expenses for transportation and maintenance. It is estimated that after interest and other fixed charges, the combined net deficit for the first quarter will be less than half as large as the deficit for the same quarter last year, which amounted to $44,000,000.

A group of 25 large utility systems supplying electric, gas and other services and reporting for the 12 months ended March 31 showed an increase of 6 per cent in total operating revenues as compared with the corresponding period last year but, because of higher operating expenses and taxes, an increase of only 5 per cent in net income.

American Telephone & Telegraph Company and its principal telephone subsidiaries, reporting for the 12 months ended February 29, had an increase of about 6 per cent in operating revenues, and an increase of 23 per cent in net income (due in part to increased earnings this year of its non-telephone subsidiaries). Taxes upon the Bell System rose to a new high for the period, amounting to over 13 per cent of total revenues or 76 per cent of net income (after taxes), and were almost four times interest charges.

The National City Bank of New York

Head Office · 55 WALL STREET · *New York*

Condensed Statement of Condition as of March 31, 1940

INCLUDING DOMESTIC AND FOREIGN BRANCHES

ASSETS

Cash and Due from Banks and Bankers		$1,145,377,321.71
Gold Abroad or in Transit		2,596,741.00
United States Government Obligations (Direct or Fully Guaranteed)		729,182,696.27
Obligations of Other Federal Agencies		39,152,109.24
State and Municipal Securities		125,841,379.65
Other Securities		64,440,472.92
Loans, Discounts and Bankers' Acceptances		538,035,167.15
Real Estate Loans and Securities		8,136,494.43
Customers' Liability for Acceptances		11,796,117.57
Stock in Federal Reserve Bank		3,900,000.00
Ownership of International Banking Corporation (Including Paris Office)		8,000,000.00
Bank Premises		42,293,728.49
Other Real Estate		470,394.81
Other Assets		1,167,154.37
Total		$2,720,389,777.61

LIABILITIES

Deposits		$2,526,408,907.27
Liability on Acceptances and Bills	$32,628,018.16	
Less: Own Acceptances in Portfolio	16,110,859.98	16,517,158.18
Items in Transit with Branches		16,478,856.19
Reserves for:		
Unearned Discount and Other Unearned Income		4,012,020.38
Interest, Taxes, Other Accrued Expenses, etc.		9,188,600.42
Dividend		1,550,000.00
Capital	$77,500,000.00	
Surplus	52,500,000.00	
Undivided Profits	16,234,235.17	146,234,235.17
Total		$2,720,389,777.61

Figures of Foreign Branches are as of March 25, 1940.

$65,231,031.93 of United States Government Obligations and $20,201,085.51 of other assets are deposited to secure $58,827,151.89 of Public and Trust Deposits and for other purposes required by law.

(Member Federal Deposit Insurance Corporation)

City Bank Farmers Trust Company

Head Office · 22 WILLIAM STREET · *New York*

Condensed Statement of Condition as of March 31, 1940

ASSETS

Cash and Due from Banks	$ 50,623,905.68
United States Government Obligations (Direct or Fully Guaranteed)	30,328,234.11
Obligations of Other Federal Agencies	3,513,584.21
State and Municipal Securities	7,948,275.08
Other Securities	2,330,569.94
Loans and Advances	5,598,525.39
Real Estate Loans and Securities	5,192,675.13
Stock in Federal Reserve Bank	600,000.00
Bank Premises	3,986,786.25
Other Real Estate	610,503.79
Other Assets	1,595,595.72
Total	$112,328,655.30

LIABILITIES

Deposits	$ 85,749,684.62
Reserves	1,664,469.95
Capital	10,000,000.00
Surplus	10,000,000.00
Undivided Profits	4,914,500.73
Total	$112,328,655.30

$1,520,000.00 of United States Government Obligations are deposited with public authorities for purposes required by law.

(Member Federal Deposit Insurance Corporation)

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